

## Message Text

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TO SECSTATE WASHDC 487

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E.O. 11652: N/A

TAGS: ETRD, CIEC, EEC

SUBJECT: EC PREPARATIONS FOR THE DIALOGUE ON RAW MATERIALS-  
INDEXATION

REF: 75 EC BRUSSELS 9300

1. BEGIN SUMMARY: THE EC COMMISSION HAS PREPARED A WORKING PAPER ON THE INDEXATION OF PRICES OF RAW MATERIALS IN PREPARATION FOR THE CIEC COMMISSION ON RAW MATERIALS (CORM). (COPIES OF THE PAPER PLUS INITIAL EC COUNCIL WORKING GROUP COMMENTS HAVE BEEN SENT TO EUR/RPE, ATT: CASEY.) THE PAPER ARGUES THAT (A) IT HAS NOT BEEN PROVEN THAT THERE HAS BEEN AN OVERALL DETERIORATION IN THE TERMS OF TRADE FOR RAW MATERIALS AND (B) A SYSTEM OF GENERALIZED INDEXATION OF PRICES OF RAW MATERIALS WOULD NOT BE AN EFFECTIVE WAY OF HELPING TO STABILIZE OR IMPROVE THE DEVELOPING COUNTRIES' INCOMES. END SUMMARY.

2. TERMS OF TRADE - THE COMMISSION PAPER, AFTER DESCRIBING THE TECHNICAL AND CONCEPTUAL COMPLEXITIES OF ARRIVING AT A MEANINGFUL TERMS OF TRADE ANALYSIS, NOTES THE CONCLUSIONS  
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OF THE UNCTAD WORKING PARTY (APRIL 28-MAY 1, 1975) THAT AVAIL-

ABLE STATISTICS DID NOT BEAR OUT THE THESIS THAT THE DEVELOPING COUNTRIES NET "BARTER" TERMS OF TRADE WERE TENDING TO DETERIORATE. IT USES TABLES OF UNCTAD AND THE WORLD BANK (FOUND IN ANNEXES FROM WHICH IT DRAWS THE CONCLUSION THAT THE LONG-TERM TREND OF "BARTER" TERMS OF TRADE FOR ALL DEVELOPING COUNTRIES WERE VERY FAVORABLE OVERALL BUT WHEN THE OIL EXPORTING COUNTRIES ARE EXCLUDED, THERE IS A SLIGHT DETERIORATION. HOWEVER, IT POINTS OUT THAT THE TREND OF THE "INCOME" TERMS OF TRADE INDEX UP TO 1974 WAS FAVORABLE, EVEN IF OIL EXPORTERS ARE EXCLUDED. ("INCOME" TERMS OF TRADE IS DEFINED AS THE NET BARTER TERMS OF TRADE MULTIPLIED BY AN INDEX OF THE VOLUME OF EXPORTS.) NONETHELESS, "INCOME" TERMS OF TRADE FOR THE POOREST DEVELOPING COUNTRIES SEEM TO HAVE DETERIORATED AS, SURPRISINGLY, DID THE "BARTER" TERMS OF TRADE FOR DEVELOPING COUNTRIES WHICH EXPORT MANUFACTURED GOODS.

3. INDEXATION - THE COMMISSION PAPER ARGUES THAT INDEXATION OF COMMODITY PRICES POSES A SERIES OF DIFFICULTIES WHICH MAKE ITS ADOPTION UNDESIRABLE. SOME OF THE ECONOMIC ARGUMENTS AGAINST INDEXATION ARE (A) PRICES BASED ON INDEXATION RATHER THAN MARKET FORCES WOULD REQUIRE COSTLY MANIPULATION OF SUPPLY, I.E., CONCERTED MANAGEMENT OF PRODUCTION, BUFFER STOCKS, ETC.; (B) LOW COST PRODUCERS COULD NOT INCREASE THEIR MARKET SHARES AND HIGH-COST PRODUCERS WOULD NOT SHIFT RESOURCES TO OTHER PRODUCTIVE ACTIVITIES; AND (C) THERE WOULD BE OVER OR UNDER-INVESTMENT, DEPENDING ON THE FIXED LEVEL OF PRICES.

4. A SECOND MAJOR PROBLEM IS THE TERMS OF REFERENCE TO BE USED FOR THE INDEXATION. IT IS NOT CLEAR WHETHER INDEXATION SHOULD BE BASED ON: (A) LINKING PRICES OF LDC IMPORTS TO EXPORTS; (B) LINKING PRICES OF LDC RAW MATERIAL EXPORTS TO IMPORTS OF MANUFACTURED GOODS; (C) LINKING PRICES OF RAW MATERIAL EXPORTS TO THE PRICES OF MANUFACTURED GOODS IN WHICH THEY ARE INCORPORATED; AND (D) LINKING PRICES OF RAW MATERIALS TO PRODUCTION COSTS OR COSTS OF SUBSTITUTES. THE PAPER THEN DESCRIBES THE INEQUITIES TO CERTAIN LDCS IF "ALL" RAW MATERIALS ARE NOT INDEXED AS WELL AS THE ADDITIONAL BURDENS TO LDCS IMPORTING RAW MATERIALS IF RAW MATERIALS ARE INDEXED. THE PAPER ALSO POINTS OUT THAT WHILE ANY INDEXATION FORMULA RAISES AWKWARD STATISTICAL PROBLEMS, THEY ARE PARTICULARLY COMPLICATED LIMITED OFFICIAL USE

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IF PRICE INDICES ARE DRAWN UP FOR DEVELOPING COUNTRIES' IMPORTS AND EXPORTS. IT DEMONSTRATES THAT ANY APPROACH RESULTS IN INEQUITIES BETWEEN THE RAW MATERIAL EXPORTING COUNTRIES.

5. THE PAPER CONCLUDES THAT INDEXATION IS NOT AN EFFECTIVE MECHANISM FOR STABILIZING AND INCREASING THE INCOME OF THE DEVELOPING COUNTRIES IN THE MEDIUM TERM. IT HOLDS THAT SOLUTIONS SHOULD BE SOUGHT THROUGH COMMODITY AGREEMENTS, ORGANIZATION

OF MARKETS, COMPENSATORY FINANCING, OPENING DEVELOPED COUNTRY MARKETS, ETC. IN THIS CONNECTION, IT ACCEPTS THE POSSIBILITY THAT IN THE CONTEXT OF COMMODITY AGREEMENTS OR MEASURES TO STABILIZE EXPORT EARNINGS FROM RAW MATERIALS, PRICE REVISION METHODS MIGHT BE EMPLOYED.

6. EC COUNCIL WORKING GROUPS ON RAW MATERIALS AND DEVELOPMENT HAVE DISCUSSED THE ABOVE PAPER. THERE WAS GENERAL AGREEMENT BY THE MEMBER STATES WITH THE COMMISSION ANALYSIS AND ITS CONCLUSION THAT "INDEXATION WAS NOT THE MOST APPROPRIATE MEANS TO SOLVE THE PROBLEMS OF THE LDCS CAUSED BY FLUCTUATIONS IN RAW MATERIAL PRICES." THE IRISH AND DUTCH DELEGATIONS RESERVED THEIR POSITION ON GROUNDS THAT THE EC SHOULD AWAIT THE RESULTS OF UNCTAD STUDIES ON THE SUBJECT. A NUMBER OF DELEGATIONS EXPRESSED AN INTEREST IN NON-AUTOMATIC ADJUSTMENTS OF PRICES SUCH AS PRICE REVISION CLAUSES IN COMMODITY AGREEMENTS.  
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## Message Attributes

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**Disposition Approved on Date:**  
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**Disposition Comment:** 25 YEAR REVIEW  
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